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C O N F I D E N T I A L SECTION 01 OF 03 MEXICO 002637

SENSITIVE
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NSC FOR SENIOR DIRECTOR RESTREPO;DEPT FOR WHA DAS JACOBSON
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SUBJECT: MEXICO: BUDGET, ECONOMIC ISSUES LIKELY TO DOMINATE
THE NEW CONGRESS

REF: A. MEXICO 2537

[1](#)B. MEXICO 002340

[1](#)C. MEXICO 001993

Classified By: Confidential by Political Minister Counselor Gustavo
Delgado. Reason: 1.4 (b),(d).

[1](#)1. (C) Summary. The Mexican legislative session opened on September 1 with new players and a dramatically changed political landscape, following the July midterm elections. With the opposition Institutional Revolutionary Party (PRI) now the largest party in the lower house -- the PRI has 237 seats to the National Action Party's (PAN) 143 -- the Calderon government will have to raise its game on crucial budget negotiations at a time of continuing economic crisis and significant internal security challenges. In the coming months and years we are likely to see hard fought political battles and little progress on major structural reforms. Presidential ambitions in the run up to 2012 will shape much of the debate, with the major parties and potential candidates gearing policy proposals mostly for maximum electoral advantage. End Summary

Legislative Priorities: Budget and Economics...

[1](#)2. (C) Budget negotiations and managing Mexico's economic crisis are likely to all but consume this four-month session, with each of the three major parties looking to hone their financial credentials in the debates. With its almost absolute majority in the Chamber of Deputies, which has sole approval authority over the expenditure bill, the PRI will have considerable influence over the budget process. The GOM will submit the budget to Congress on September 8, and the Chamber will have until November 15 to approve the expenditure bill. With a 2.7 percent of GDP spending gap for 2010, President Calderon is proposing austere measures that will likely include a combination of debt, some higher taxes, and lower spending to manage the budget (ref a). Administration officials have made a case for fiscal reform, but while observers see the possibility for some tinkering around the margins, a comprehensive reform is unlikely to pass muster with the PRI and Revolutionary Democratic Party (PRD).

[1](#)3. (C) Since its July electoral victory, the PRI has backed down somewhat from its initial stance against any tax

increases, but observers say the party still favors incurring more debt and strengthening social programs over expenditure cuts and significant tax increases. Analysts also say that new PRI Chamber coordinator, Francisco Rojas, is an adept administrator who will be able to find areas in the budget to make small, less costly cuts that nevertheless will help the party make the case for few tax hikes. The party will advocate greater transfers to the states -- PRI currently controls 19 of 32 (including the Federal District) and will face elections in ten, mostly PRI-controlled states in 2010 -- to take the economic heat off of their governors. It will also likely push for a lower benchmark oil price so that a greater portion of the resulting surplus would go to the states for discretionary spending. On September 2, the PRI presented to the Chamber its 83 point economic recovery package, which reportedly includes poverty reduction and job creation measures, as well as more dramatic proposals such as a plan for universal health insurance. The party has said it continues to oppose a VAT tax on food and medicines, but is in wait-and-see mode for the President's budget and economic packages. PRD interlocutors have said the party will advocate for increased social spending and the rejection of any new taxes.

...Security...

14. (C) The past three years have seen a flurry of congressional and executive activity on a variety of important reforms aimed at better equipping the Mexican state to confront the country's security challenges. This session

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will feature more rhetorical fireworks as the parties, particularly the PRI, seek to score points off of the GOM for Mexico's security struggles. In general, however, the parties will negotiate behind the scenes and probably reach agreements on a number of outstanding security-related proposals. The PRI and PRD may use their support for Calderon's security efforts as bargaining chips in other debates, particularly those related to the economy and budget. Key legislation that Congress will consider this session includes the passage of the criminal procedural codes necessary to move Mexico to an accusatorial justice system, the development of a federal anti-kidnapping law, and money-laundering legislation. Civil society representatives hope Congress will pass the complicated, but critical, procedural codes that have languished in the legislature since 2008. Perhaps the most contentious security topic Congress will address this session is Calderon's proposed National Security legislation that would codify the military's participation in the counternarcotics fight on Mexican soil and give the President considerable authority over their mandate. PRI and PRD interlocutors have told us that their parties will not approve the law as written and will instead look to increase congressional oversight over such matters.

15. (C) Cuts to the security budget do not appear to be in play -- unofficially, government and opposition sources have suggested they will not cut security spending. All parties, including and especially the PRI, have an interest in demonstrating their commitment to the counterdrug fight. Nevertheless, the composition of the spending package could change should the PRI shift more resources to the states and municipalities.

...And State Reform.

16. (C) PRI contacts have told us that the party will focus on state reform to strengthen Congress vis-a-vis the Presidency and further empower the states, efforts mostly driven by a Machiavellian political calculus to weaken the executive branch and bolster the PRI's legislative track record in the run-up to the 2012 presidential elections (ref b). While the

PRI is likely to face resistance from the PAN to some of these moves, efforts to modernize the legislature appear to have broad political support. Both the PAN and the PRI, as well as at least some PRD elements, have said they will propose measures to reduce the size of both chambers and to allow for limited re-election. The PAN will also press for greater transparency from government functionaries at the federal and state level, and Congress will consider laws to limit legislators' discretionary expenditures, such as imposing stricter controls on purchasing airline flights, and allow for exhaustive reviews of their finances. Most observers note that proposals to modernize Congress could help move forward Mexico's democratic transition and encourage needed introspection by legislators of their own behavior. Nevertheless, the PRI's hopes of granting the states even more political and economic power run the risk of reinforcing already problematic tendencies. This includes increased use of social spending for political gain and inefficient spending practices, as state leaders already lack the infrastructure and capacity to absorb effectively federal transfers in some localities.

Energy and Labor Reform Touchy Subjects

17. (C) While Josefina Vazquez Mota has said that nothing is off the table and Calderon in his State of the Union Address on Tuesday said that energy and labor reform are necessary to transform Mexico (see septel), serious changes to these sectors seem at this point highly unlikely this session. PRI leaders have told us on a number of occasions that the party is unwilling to take legislative risks that could jeopardize its public standing (energy reform) or exacerbate party divides (labor reform). PRI Senate leader Manlio Fabio Beltrones said on Tuesday that the PRI continues to oppose

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another energy reform that would move Mexican state oil company PEMEX closer to privatization. The PRI might be able to sign on to non-controversial reforms that tinker around the edges, but will almost certainly reject a major labor or energy overhaul as too risky in the run-up to the 2012 vote..

Alliances and Strategy

18. (C) All parties have publicly pledged to work responsibly together this legislative session, and incoming PRI deputy Luis Videgaray told Emboffs to expect more communication between the groups than what appears in press. Many -- including PRI deputy Carlos Flores Rico -- have interpreted the selection of Francisco Rojas as Chamber PRI coordinator as a sign that the PRI will continue to work with the PAN and President Calderon on key issues. Flores Rico told Poloff that Rojas and his close associate, Mexico State Governor Enrique Pena Nieto, hail from a faction that favor more conciliatory relations with the PAN, and observers note that Rojas is an able politician who will be able to aptly negotiate with the President and his party.

19. (C) Nevertheless, local analysts suggest that the PRI will try to score public relations points by driving the Chamber's agenda. The PRI will attempt to do so by making only minor proposals so as not to aggravate internal divisions that so damaged the party during the years under President Fox. The PRI is unlikely to maintain its over 90 percent voting coincidence with the PAN, and has told us it will look more toward the PRD for support. The PRI is certain to vote, however, with the PAN on pragmatic issues of shared interest, particularly relating to security proposals to improve intelligence coordination and money laundering. The PAN and PRD may also look to increase cooperation as a means to check PRI attempts to score political points. PRD Senator Tomas Torres told Poloff that his party will work with both of the other major parties, seeing this as the best way for the PRD to have influence in the congressional debate

given its much-reduced presence in the Chamber. The PRI will also not be able to rely on the Green Party for unconditional support; the Green Party has said it will only maintain an issue-specific alliance, and PRI representatives have told us the party also will not back the Green Party on every proposal. (ref c)

Comment

¶10. (C) Most political capital, time, and negotiating energy will be dedicated to the budget and economic debate this session. President Calderon and his PAN party will be looking for pragmatic solutions to address Mexico's fiscal problems, while the PRI will seek to capitalize on its July electoral success and lay the groundwork for a 2012 presidential bid. The PRD will struggle to maintain its political relevance, perhaps by making alliances when it can and holding itself together as a single legislative force. Major structural reforms, particularly economic, energy, or labor, are unlikely over the next four months and are difficult to foresee in the next three years. The PRI will cautiously maneuver to secure compromises from its opponents, such as increased funds to the states and support for its agrarian programs, without risking alienating voters or exacerbating its own internal divisions. The PAN will try to carefully balance improving Mexico's economic structure through measures like increased tax collection or moderate fiscal reform while still recapturing public support following its electoral defeat. Presidential ambitions will shape much of the debate, with the major parties and potential candidates gearing policy proposals mostly for maximum electoral advantage. Visit Mexico City's Classified Web Site at <http://www.state.sgov.gov/p/wha/mexicocity> and the North American Partnership Blog at <http://www.intelink.gov/communities/state/nap/>

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